

STATEMENT OF
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U.S. DEPARTMENT OF TRANSPORTATION
BEFORE THE COMMITTEE ON PUBLIC WORKS AND TRANSPORTATION
SUBCOMMITTEE ON SURFACE TRANSPORTATION
U.S. HOUSE OF REPRESENTATIVES
REGARDING FREIGHT FORWARDER DEREGULATION
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Mr. Chairman and Members of the Committee, thank you for inviting me here today to discuss the Department of Transportation's views regarding freight forwarder deregulation.

FREIGHT FORWARDER REGULATION IS OUTDATED

Although the Motor Carrier Act of 1980 (MCA) has provided significant new operational freedoms and reduced regulatory burdens for common and contract motor carriers, most of these benefits have yet to be provided to freight forwarders. It has been over forty years since the basic framework of freight forwarder regulation was devised. The regulatory framework of 1942 is ill-suited to the transportation realities of 1986. Strict freight forwarder regulation is particularly anomalous in an era of transportation deregulation and its concomitant market changes. Freight forwarder deregulation is dictated by equity considerations as well as by the principles of economic efficiency.

We believe that the regulatory changes proposed by S. 1124 are especially worthy of support. It is very similar to our bill submitted to Congress in September 1985, but not yet introduced.

FREIGHT FORWARDERS AND THEIR COMPETITORS

Who are the members of this "forgotten segment" of trucking, and how do they compare with other segments of the surface

transportation industry? In many ways, forwarders are similar to shippers' associations and brokers. Like the former, they consolidate shipments in order to take advantage of truckload rates; like the latter, they bring shippers and carriers together and help meet the informational needs of smaller shippers. However, unlike either, forwarders are common carriers and, as such, are subject to more stringent regulation than either shippers' associations or brokers.

There are also many similarities between less-than-truckload (LTL) motor carriers and freight forwarders, both of whom consolidate LTL shipments into truckload lots. Like LTL common carriers, freight forwarders have benefited from easier entry policies. Also like motor common carriers, forwarders must publish and file their tariffs with the Interstate Commerce Commission (ICC). However, unlike their motor common carrier counterparts, they cannot hold "dual operating authority" and also serve as contract carriers exempt from tariff filing requirements. In addition, a freight forwarder is not permitted to provide the line-haul transportation for its shipments but, rather, must purchase this transportation from motor carriers or railroads.

The freight forwarder, as we know it today, is substantially a product of regulation -- the regulation of over forty years ago. We strongly believe that the time to modernize that regulation has come and that it is time to offer to freight forwarders the same flexibilities and freedoms that are now enjoyed by other segments of the transportation industry against whom they compete.

Forwarders have no economic characteristics warranting regulation for efficiency reasons, such as substantial fixed costs and scale economies. Fixed assets and shareholders' equity for even the largest freight forwarders averaged only slightly over one million dollars in 1978. The only historical basis for their regulation was to provide consistency with the regulation of other freight modes -- railroads, trucks, and barges -- at the time the controls were instituted with the Freight Forwarder Act of 1942. Furthermore, forwarders must now compete on inequitable terms with other types of rapidly expanding third parties -- shippers' associations, shippers' agents, and property brokers -- which are virtually unregulated. These entities are variously referred to as third parties, intermediaries, and middlemen. The terms are thus used interchangeably in this statement.

CHANGES IN TRANSPORTATION MARKETS SINCE 1980

In 1980, enactment of the MCA and the Staggers Rail Act (SRA) provided substantial deregulation of the motor carrier and railroad industries and resulted in a number of critical changes in the provision of transportation services. In the trucking industry, the freer entry brought about by the MCA has resulted in entry by new carriers, expansion into new markets by existing carriers, and greater price competition. This effect was intensified by the softening of demand and the resulting buyers' market associated with the general economic slowdown of the early 1980's. These developments have been further associated with greater pricing volatility, a dampening of inflationary rate increases, and some absolute LTL rate reductions. For example, a

study conducted by Thomas G. Moore, now with the Council of Economic Advisors, found an average reduction of about 15 percent in LTL rates since the MCA.

An additional development associated with freer entry is a weakening of the rather rigid segmentation that has traditionally characterized some parts of the transportation industry's structure. This change is particularly noticeable in trucking, where the previously sharp distinctions between common and contract carriage, for-hire and private operations, and regulated and exempt services are rapidly fading. Reduced regulation has exerted a similar influence on the functional distinctions among the various types of middlemen.

Another important post-1980 development is the rapid expansion of contracting between carriers -- both rail and motor carriers -- and individual shippers, relative to traditional common carriage. Such contracting involves individual negotiations of rates and service conditions, such as the degree of liability which the carrier assumes. This change has also produced a new emphasis on large volume movements, since greater committed tonnage yields shippers more favorable contractual terms regarding prices and service.

IMPACTS ON FREIGHT FORWARDERS

These developments have a number of adverse implications for the freight forwarders. There is especially heavy competitive pressure for less-than-truckload traffic, the forwarders' mainstay, resulting in both traffic erosion and rate depression. The effect of new entry and expansion by existing motor carriers

has already been mentioned. Additional pressure may also be traced to the increased competition provided by trailer-on-flatcar (TOFC) service for truckload (TL) traffic.

TOFC service has grown rapidly since it was exempted from regulation by the Interstate Commerce Commission (ICC), pursuant to the provisions of the SRA. Increased competition for TL traffic has forced many regular route general commodity truckers to become more dependent on LTL traffic. The greater emphasis placed on LTL traffic by such carriers has cut further into the forwarders' market share and intensified rate discounting, resulting in many LTL charges which are below 1980 levels. In addition, property brokers are beginning to compete for the small shipment traffic of the forwarders and are likely to increase their share of this traffic. Forwarders are also hampered by restricted opportunities to gain from the increased emphasis on volume traffic associated with the proliferation of contract rates.

The new emphasis on volume rates enhances the importance of intermediaries, who can often consolidate shipments into volumes larger than those typically shipped by even relatively large shippers. The third-party role is also enhanced by the proliferation of price and service options, which complicates the ability of individual firms to keep up with developments. One result of contracting and its emphasis on volume shipments is the proliferation of unregulated property brokers and shippers' agents as direct competitors of the forwarders for this traffic. As an associated disability, forwarder opportunities to benefit from the

new approaches are limited by the regulatory prohibition against forwarders' contracting with either LTL or volume shippers.

Many forwarders are also disadvantaged by the asymmetry of section 11323 of the Interstate Commerce Act which prohibits their direct control of motor carriers, but does not prohibit motor carriers from acquiring direct control of freight forwarders. This anomaly limits the potential benefits of vertical integration, thus also limiting the cost savings that could be passed on to shippers and consumers. In the absence of regulatory barriers, the distinctions between forwarders and LTL trucking firms could be expected to be much less than at the present time. A basic similarity between the two types of operations is seen in the crucial character of the assembly and distribution functions which they each perform, with the ownership status of the vehicle being quite incidental to the sophisticated operations involved. Vertical integration between motor carriers and forwarders has thus been freely available to motor carriers but not to forwarders. In fact, a 1978 DOT study indicated that at least 20 of the 54 Class A general commodity freight forwarders (representing about 40 percent of the tonnage shipped) were controlled by motor carriers. In today's highly competitive environment, there is no sound policy reason to preclude forwarders from seeking the same types of benefits from integration that are available to motor carriers.

In view of the market changes that have occurred since 1980 and the special restrictions on the forwarders' ability to respond positively to them, forwarders might be expected to lag in

development behind the transport industry generally. There is some confirming evidence. As one indication, the trend in their transportation purchases from the railroads is falling well behind that of their closest counterparts, the shippers' associations. For the United States as a whole, freight forwarder total carloads dropped by about seventy-five percent since 1978, from 242,000 to 67,000.

WHY DOT SUPPORTS FREIGHT FORWARDER DEREGULATION

It should be emphasized that the proposed deregulation is not designed as an economic relief measure, and it may fail to serve that purpose. But to the extent that the forwarders' disabilities are the result of regulatory restrictions on their right to perform economically viable services, both equity and efficiency considerations dictate that the roadblocks imposed by regulation should be promptly eliminated. In order to promote both efficiency and equity objectives, forwarders must have equal flexibility in dealing with their competitors, their line-haul carriers, and their shippers.

The explicit purpose of S. 1124 is to ensure the competitiveness and efficiency of surface freight forwarder services, which the bill asserts would be fostered by the termination of the remaining ICC responsibilities for the regulation of these operators.

The proposed legislation explicitly eliminates all statutory requirements on freight forwarders of general commodities. It

thus sweeps away any artificial restraints on their ability to adapt to the market changes induced by the 1980 legislation.

In conclusion, the U.S. Department of Transportation strongly supports S. 1124 for a number of reasons:

1. It is consistent with and advances the goal of relying on market forces whenever feasible to promote competition and efficiency;
2. It advances equity and efficiency by providing forwarders with the flexibility to compete with brokers, shippers' agents, and shippers' associations on an equal basis;
3. It puts forwarders on an even footing with truckers when vertically integrated motor carrier-forwarder operations are more efficient than contracting out for the line-haul transport of freight.
4. It provides freedom to contract with shippers regarding price and service characteristics, including, for example, the degree of liability assumed;
5. It provides forwarders with the necessary flexibility to perform efficiently in transportation markets, fitting in where, how, and to the extent their performance permits. Any continuing special financial hardship experienced by forwarders would then be a reflection of economic viability and not of artificial institutional constraints;
6. It removes antitrust immunity for freight forwarder collective ratemaking, which forwarders no longer need

or want. We understand that the freight forwarders' rate bureau was disbanded at this time one year ago.

There are several changes we would recommend to S. 1124, Mr. Chairman. First, we would include brokers of freight in the reform package. While there are relatively few regulatory restrictions on brokers, compared to freight forwarders, we believe such close competitors should be able to thrive on their own merits, on the basis of what service they do offer, not what service they are allowed to offer.

Second, we would include household goods forwarders in this bill. We believe they should also be deregulated, and their claim that they cannot be deregulated until the household goods motor carriers they use are deregulated is unpersuasive. Brokers are already largely unregulated, and they have no trouble using either regulated or unregulated carriers for regulated and exempt commodities, respectively.

Third, we believe that it is no longer necessary to continue to subject these carriers to the ICC's "Carmack" provisions for carrier liability. We believe that this provision is a vestige of a regulatory system that is outdated and that ICC jurisdiction over this area is no longer needed. Today, carrier liability is covered at the state level by the provisions of the Uniform Commercial Code, which has been adopted by 49 States (all but Louisiana). Hence, the need for federally mandated uniformity seems outdated.

Now is the time to move ahead with S. 1124 and, in addition, we would urge the Committee to take up the very important and

related issue of further trucking deregulation.

Mr. Chairman, that concludes my prepared remarks. I would now be glad to answer any questions you or other Members of this Committee might have.